



**FISCAL AFFAIRS**

# **Geopolitics and Fiscal Policies in the EU**

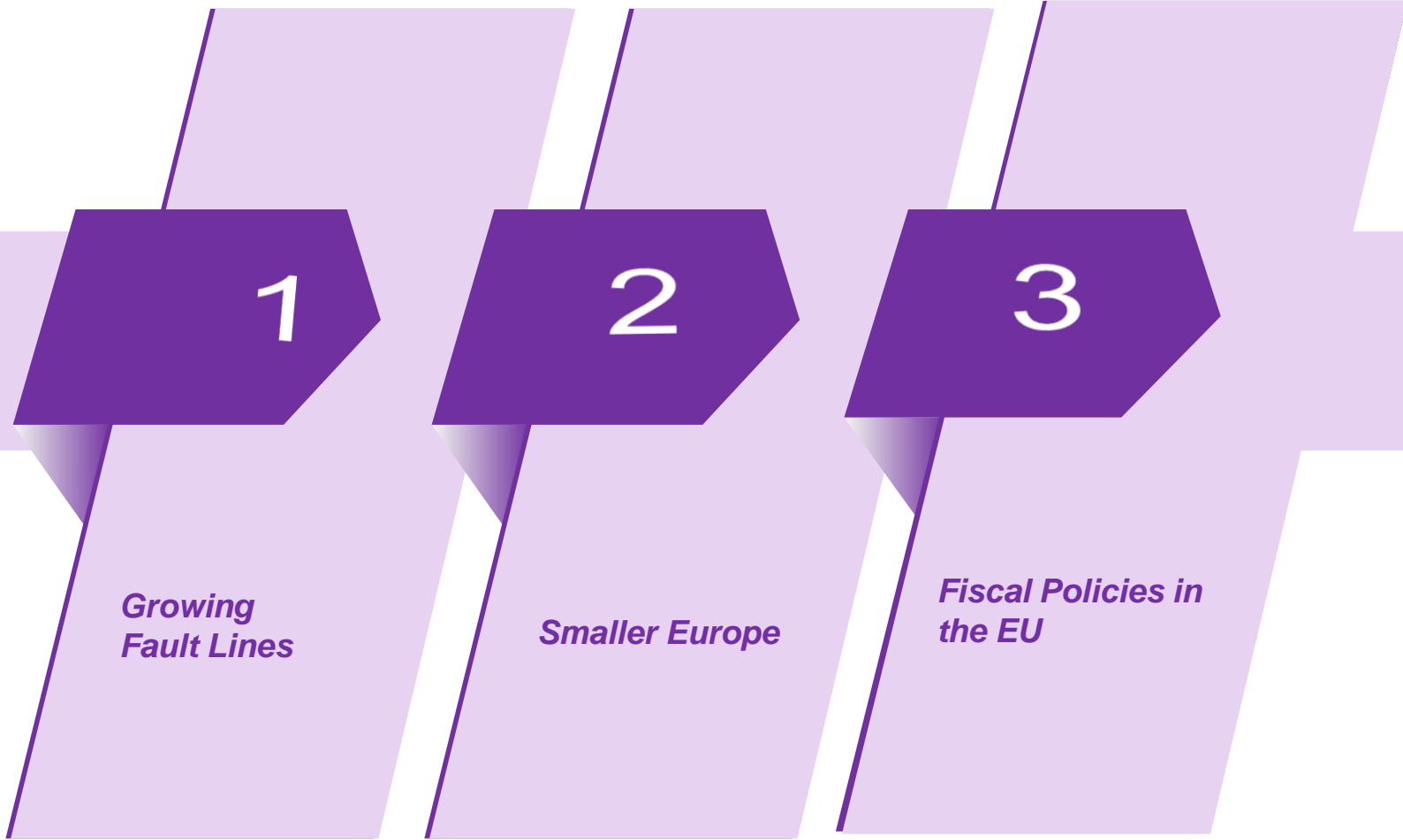
**Vitor Gaspar**  
**Director**  
**Fiscal Affairs Department**

**THE ECB AND ITS WATCHERS XXIII**

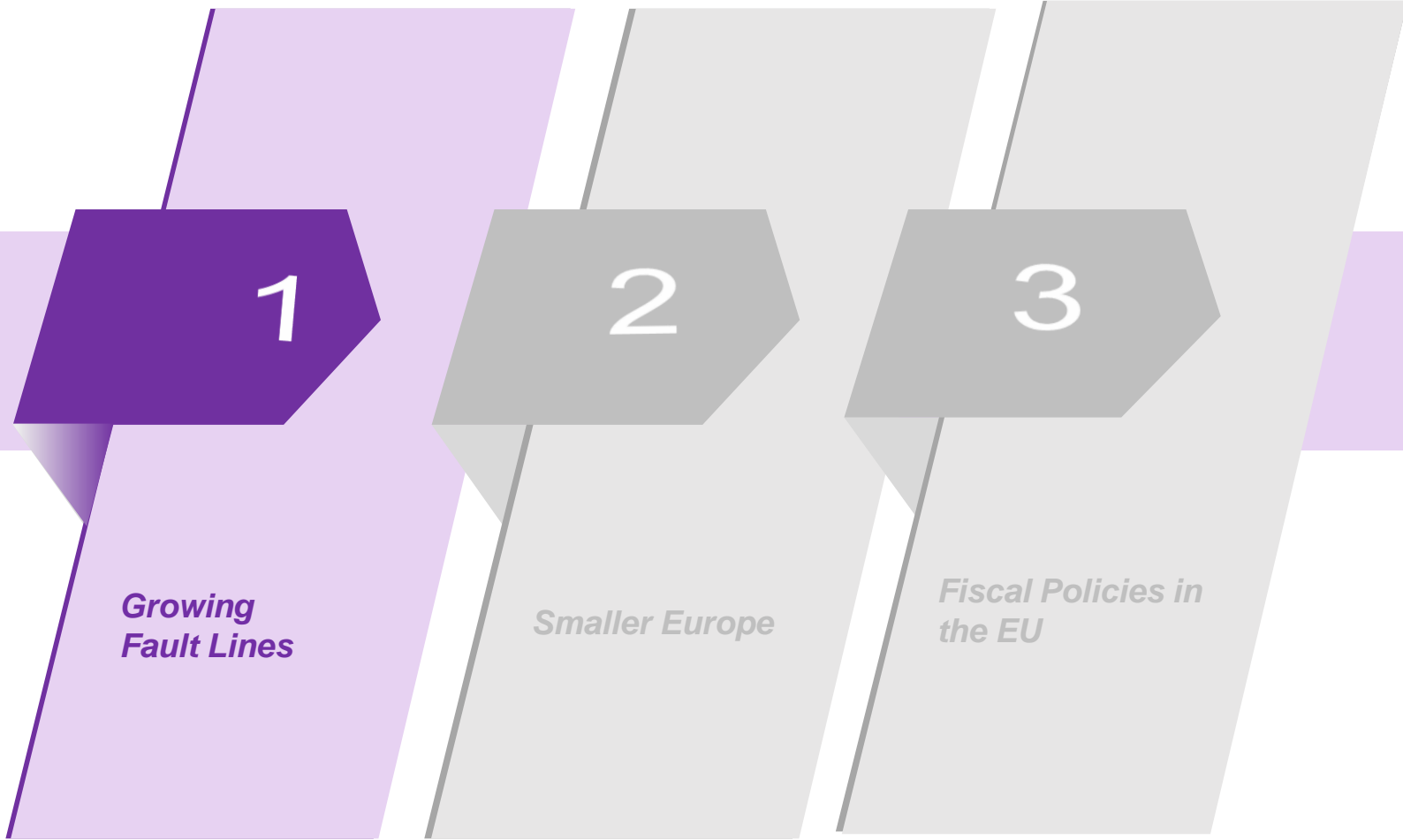
**FRANKFURT, MARCH 20TH, 2024**

The presentation was prepared by Vybhavi Balasundharam, Julieta Ladronis, and Polina Prokof'yeva. Data in the presentation uses WEO January 2024 vintage. Dates for high-frequency data are listed in the notes under the figures.

# Geopolitics and Fiscal Policies in the EU



# Geopolitics and Fiscal Policies in the EU



*Growing  
Fault Lines*

*Smaller Europe*

*Fiscal Policies in  
the EU*

# Fragmentation in the World

## Trading with friends and enemies: The threat of global fragmentation



## WTO in 'damage control' mode as Abu Dhabi agenda unravels

The failure of WTO member countries to produce anything meaningful at the group's 13th Ministerial Conference could further erode the Geneva-based organization's ability to create new global trade rules.



WTO sees signs of fragmented trade, but no de-globalisation

WTO warns about fragmentation of global trade into allied blocs

## 'Friend-shoring' set to lift prices, warns ECB

Growing number of European multinationals move production to politically friendly countries

Poland warns of further trade restrictions if deal with Ukraine not reached



New UK and EU Sanctions Introduced Against Russia

The rise of 'friendshoring' has sparked a new kind of trade war

Countries' vulnerability to food supply disruptions caused by the Russia-Ukraine war from a trade dependency perspective



China to help NEV industry respond to foreign trade restrictions

WTO chief warns on 'very costly' fragmentation of global economy

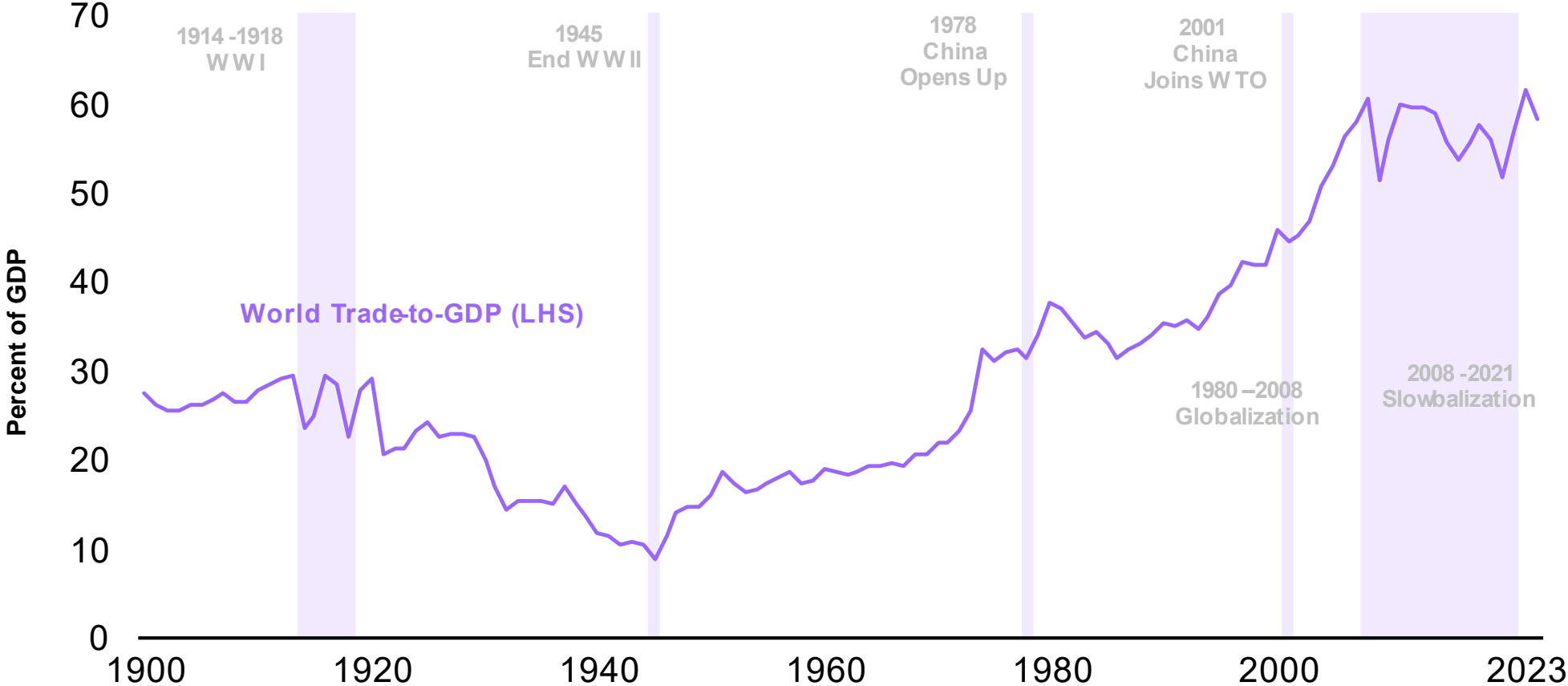
Fragmented world set to alter global trade supply chains



Global trade rift widening as Ukraine war passes two-year mark

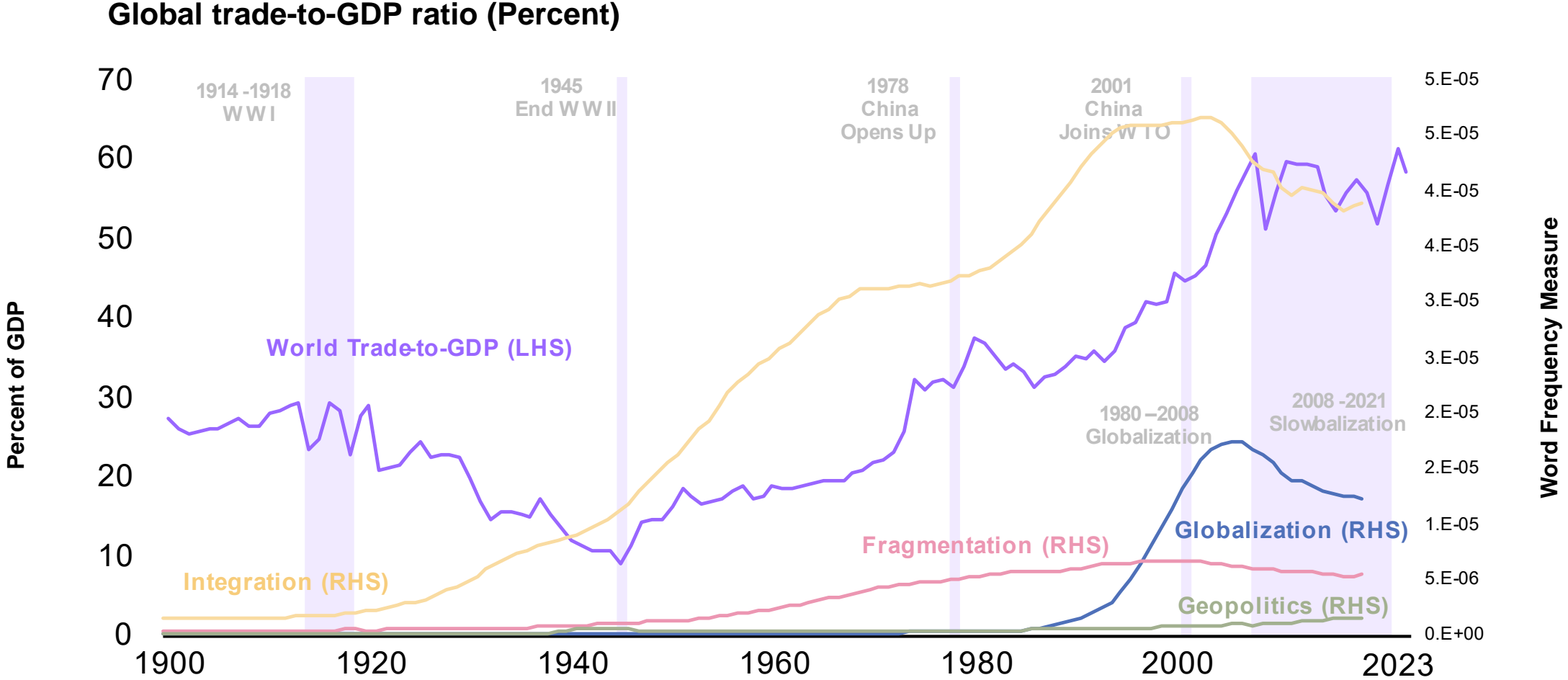
# Globalization

### Global trade-to-GDP ratio (Percent)



Sources: Cold War II? Preserving Economic Cooperation Amid Goeconomic Fragmentation. Plenary Speech by IMF First Managing Deputy Director Gita Gopinath at the 20th World Congress of the International Economic Association, Colombia. December 11, 2023

# Globalization



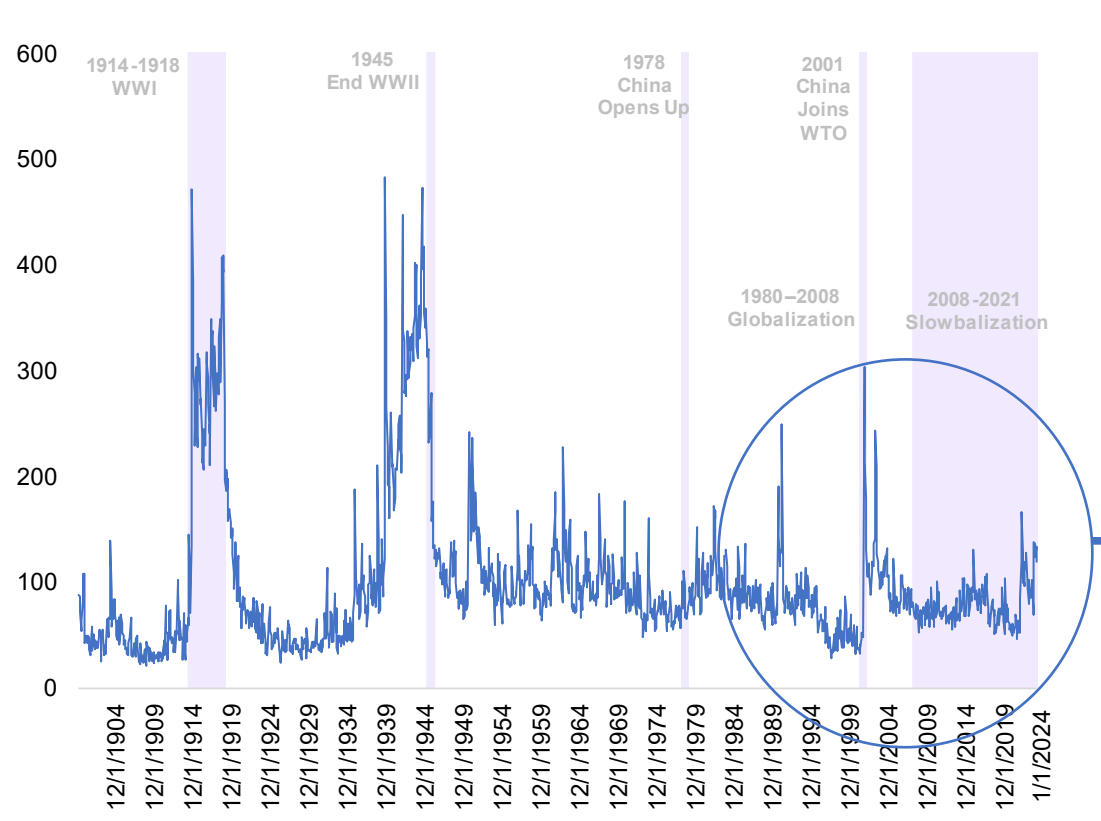
Sources: (LHS) Cold War II? Preserving Economic Cooperation Amid Goeconomic Fragmentation. Plenary Speech by IMF First Managing Deputy Director Gita Gopinath at the 20th World Congress of the International Economic Association, Colombia. December 11, 2023. (RHS) Google Ngram Viewer.

Notes: The Google Ngram Viewer is an online search engine that charts the frequencies of any set of search strings using a yearly count of n-grams found in printed sources published between 1500 and 2019.

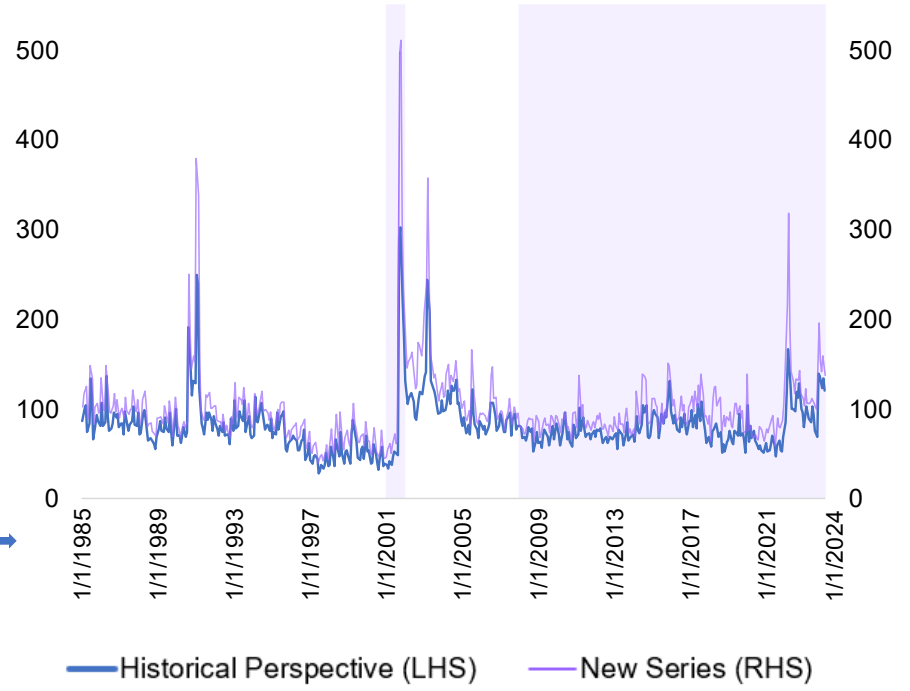


# Geopolitical Risk Index

**Historical Perspective, 1900-2024**  
(Index: 1900:2019=100)

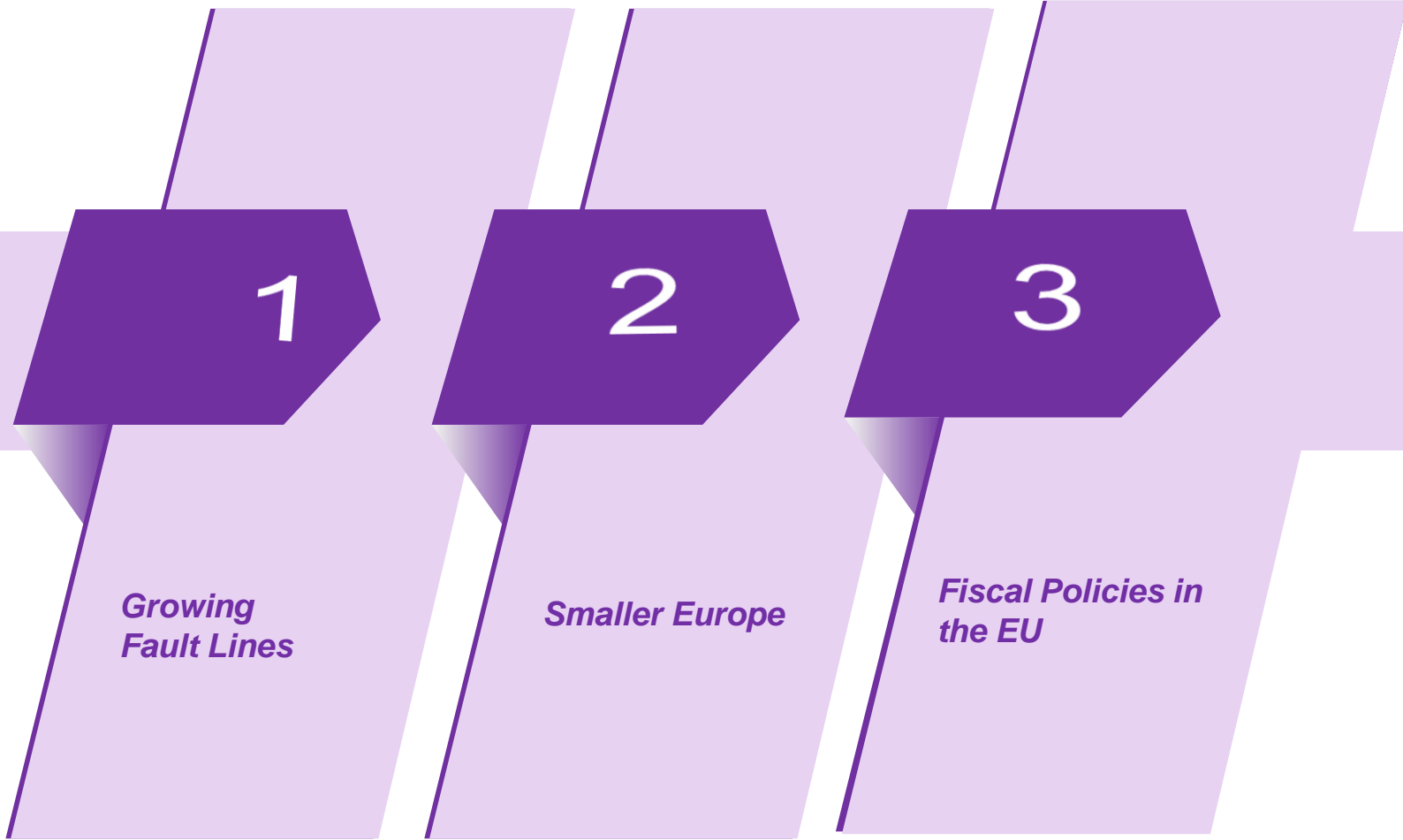


**Historical Perspective & New Series, 1985-2024**



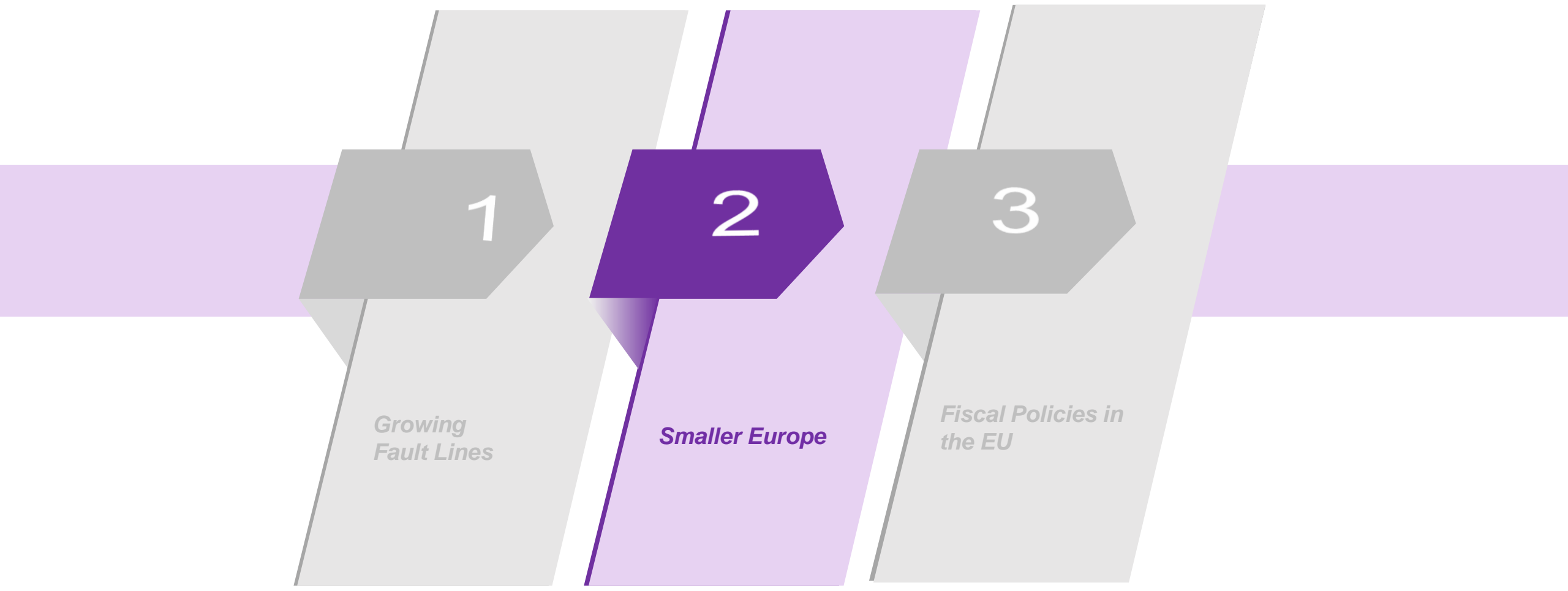
Source: Caldara and Iacoviello (2022). Data downloaded from <https://www.matteoiacoviello.com/gpr.htm> on March 08, 2024. Latest data point 2/1/2024.  
Note: The Historical Index uses 3 newspapers and starts in 1900. The Recent GPR (Index: 1985:2019=100) uses 10 newspapers and starts in 1985.

# Geopolitics and Fiscal Policies in the EU



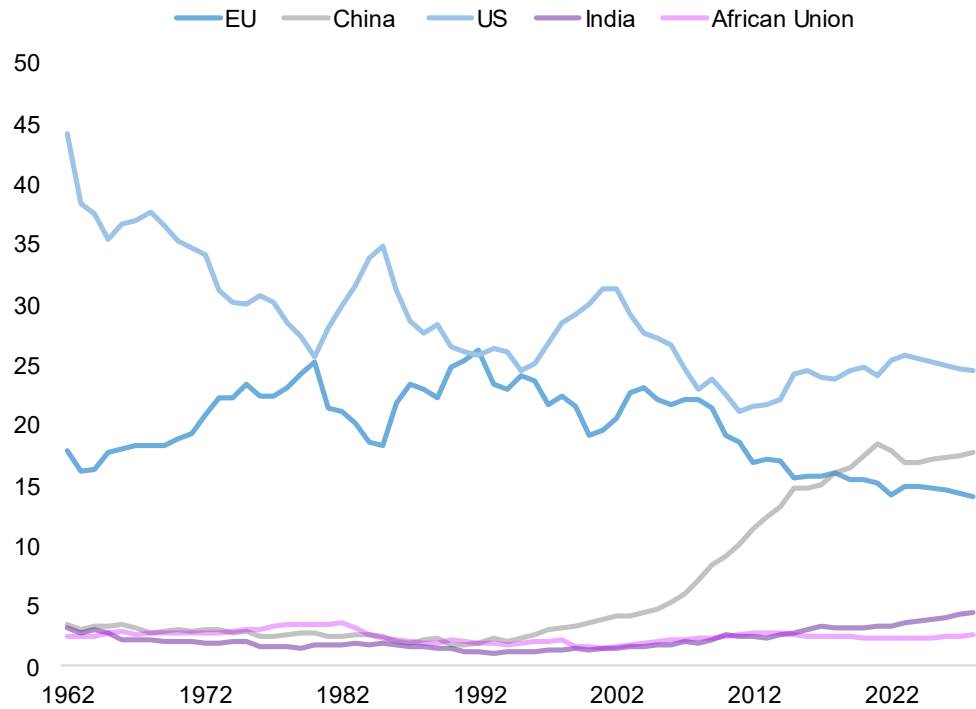


# Geopolitics and Fiscal Policies in the EU

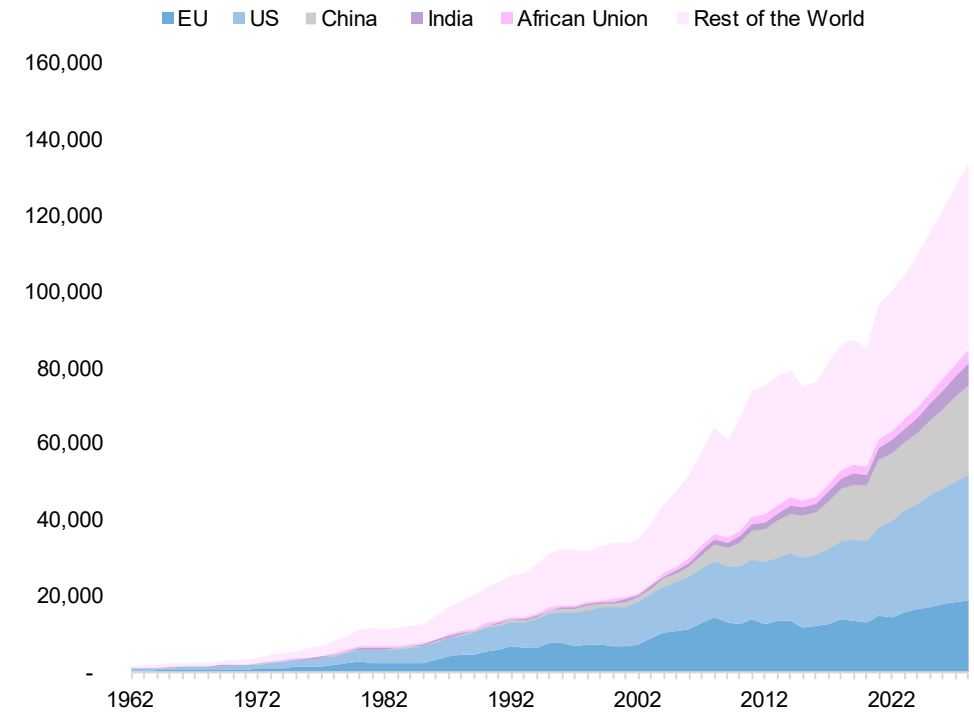


# Smaller Europe in a Growing World

## Share in the World's Economy (Percent of World GDP)



## World's GDP Constant Prices (Billion, 2017 PPP)

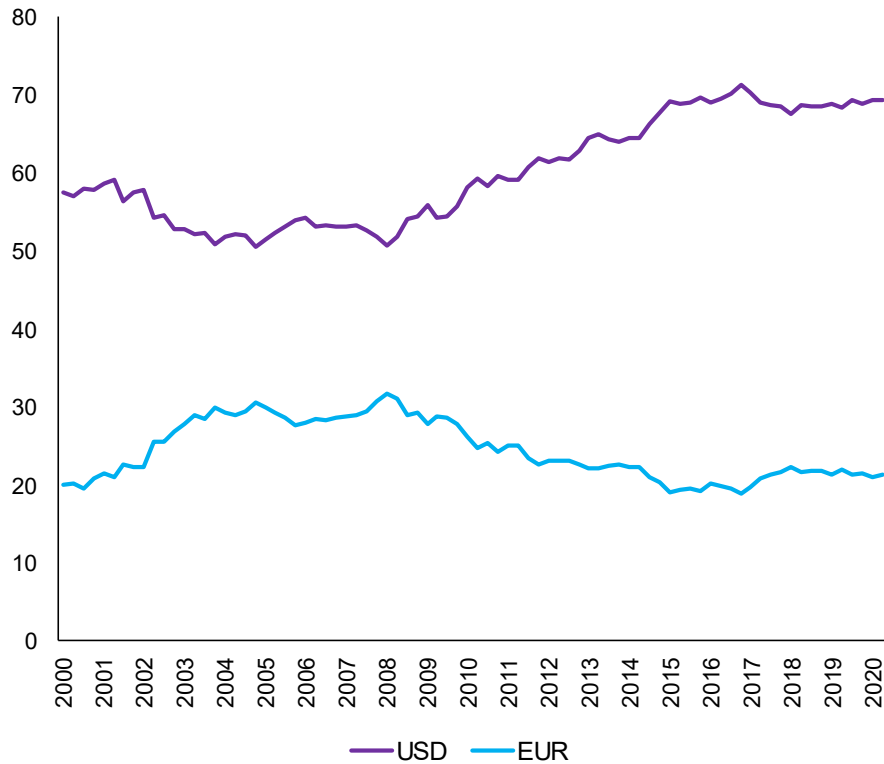


Source: IMF World Economic Outlook and IMF staff calculations.

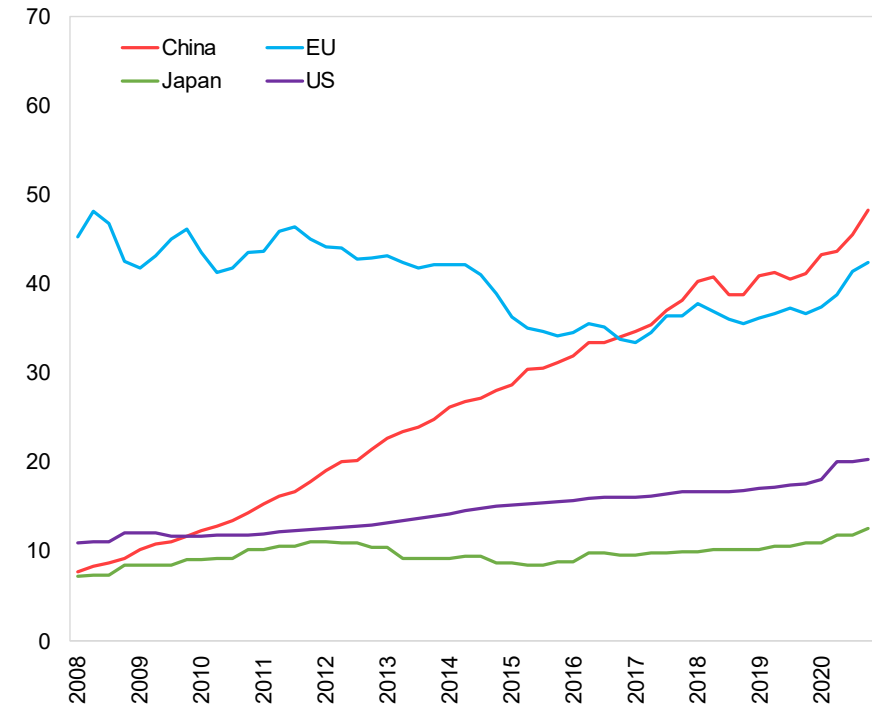
Note: Latest data point is 2028. Data are on fiscal year basis. (LHS) Shares calculated using GDP in current USD.

# Smaller Europe in the World of Finance

Currency denomination of international debt and cross-border borrowing of non-banks (Percent)

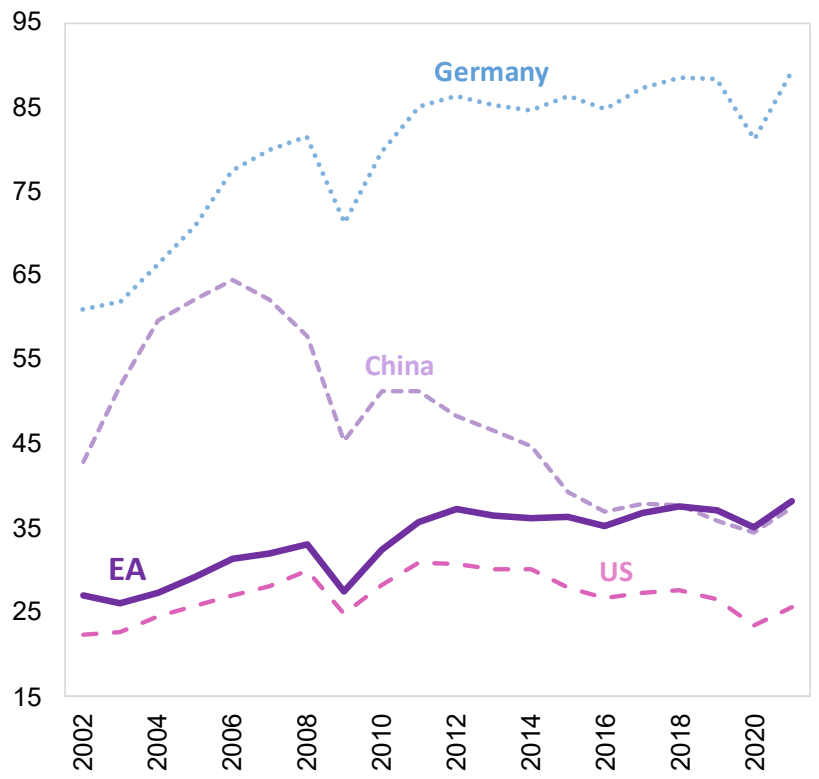


Total Bank Assets for Selected Countries (Trillion USD)

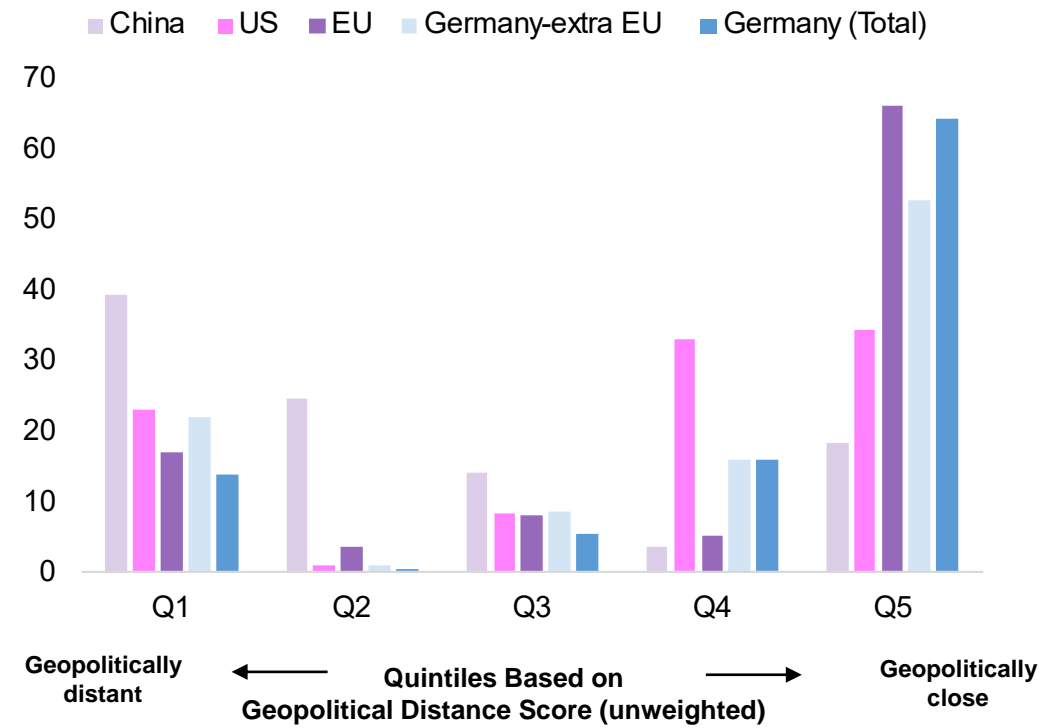


# Trade Openness

**Trade Openness  
(Percent of GDP)**

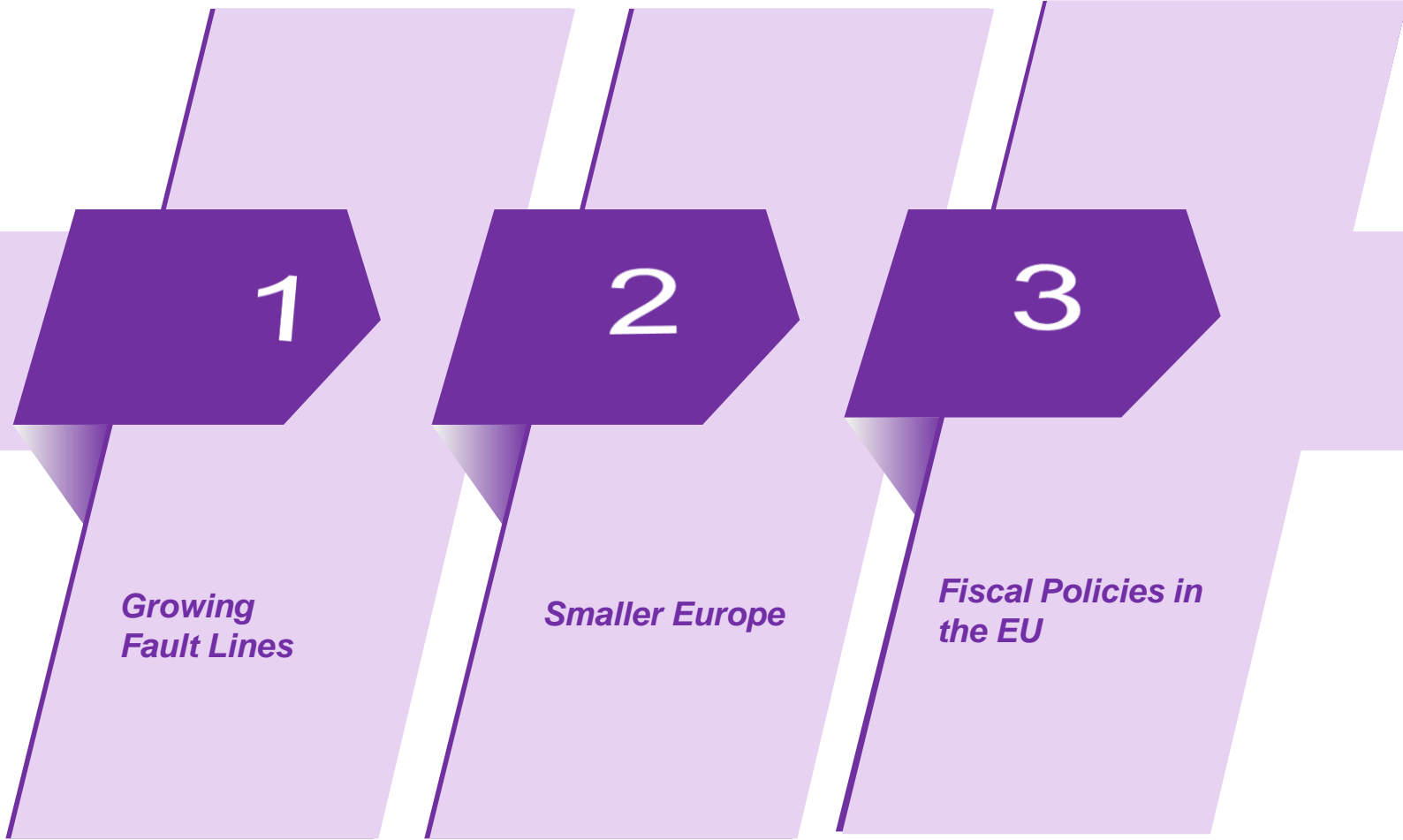


**Total Trade  
by Quintiles of Geopolitical Distance  
(Percent of Total Trade in 2021)**

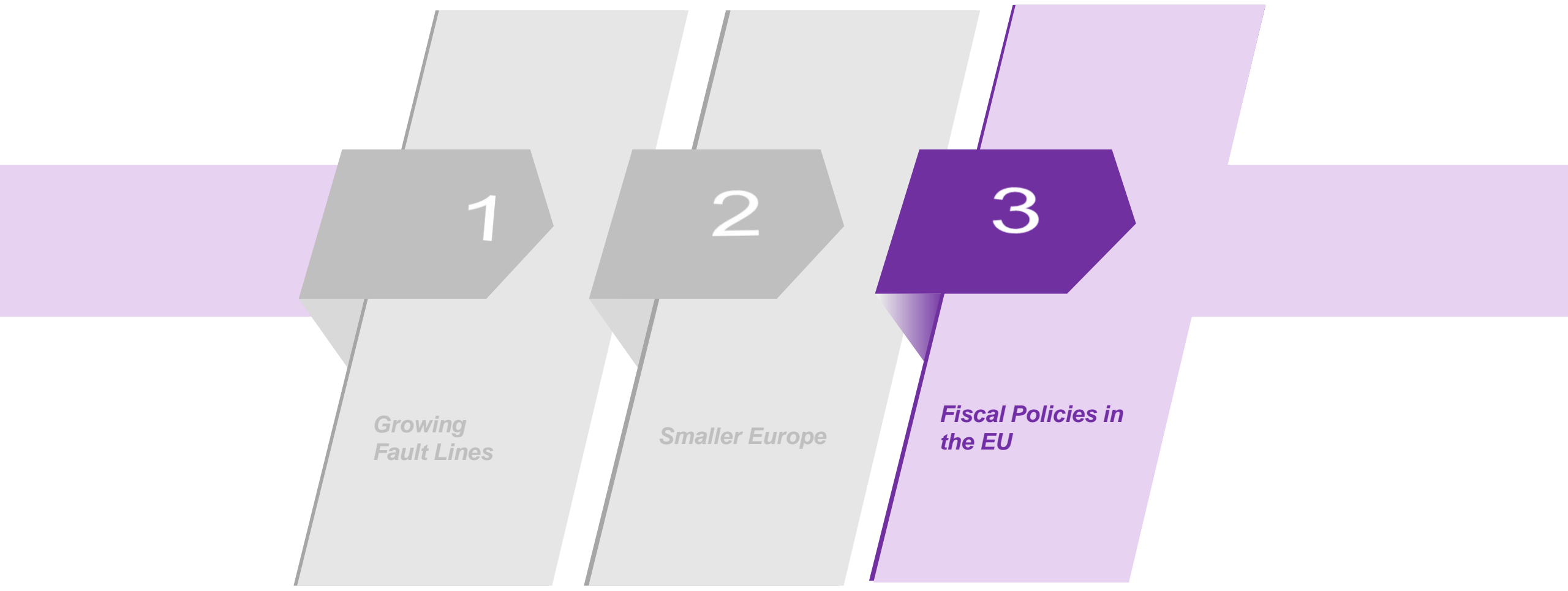


Source: (LHS) IMF World Economic Outlook, Eurostat and IMF staff calculations. (RHS) Trade-Map (UN-WTO), Voeten, Strezhnev and Bailey, Harvard Dataverse, United Nations General Assembly Voting Data & IMF staff calculations. Note: (LHS) Euro Area refers to the extra-Euro Area trade. (RHS) The measure of geopolitical distance used in the analysis is the Ideal Point Distance (IPD) constructed by Bailey and others (2017). It is based on the votes at the United Nation General Assembly between 1946 and 2021.

# Geopolitics and Fiscal Policies in the EU

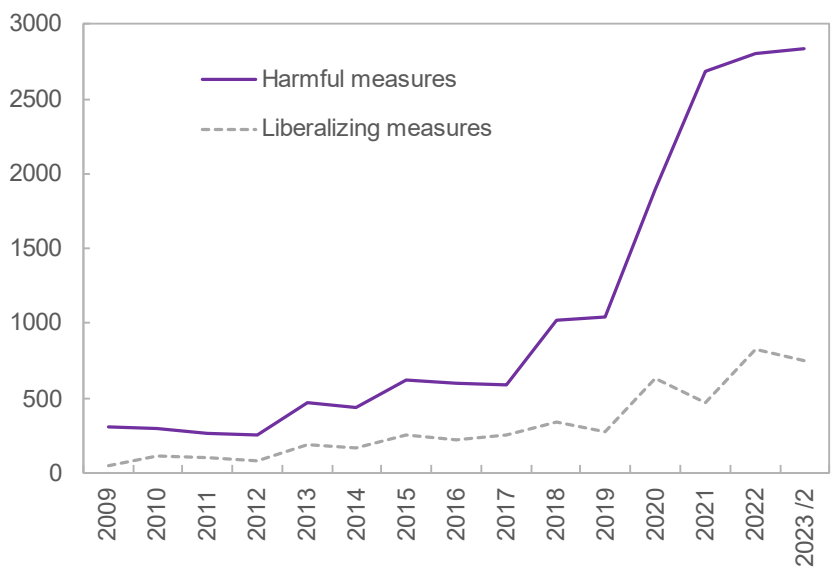


# Geopolitics and Fiscal Policies in the EU

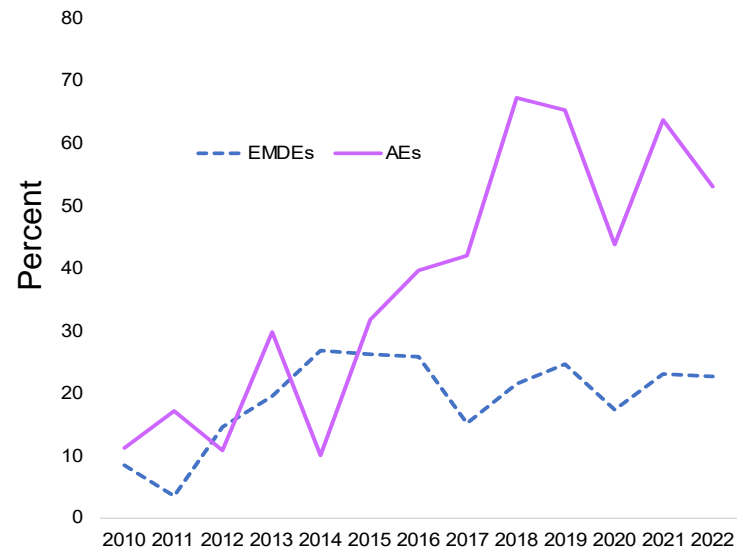


# The Rise of Industrial Policy

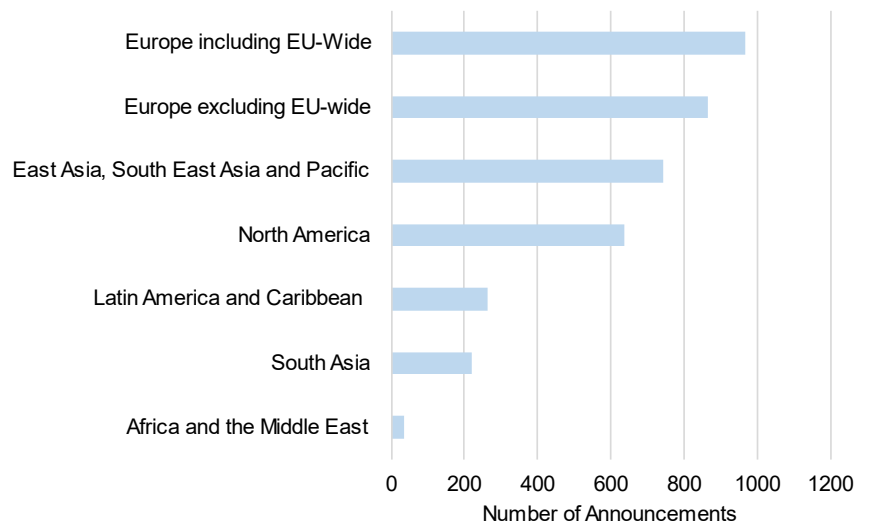
**Number of Newly Implemented Trade and FDI Restrictions**



**Industrial Policy as Share of Total Trade Policies**



**Industrial Policy: Announcements in 2023 (Number of Measures)**

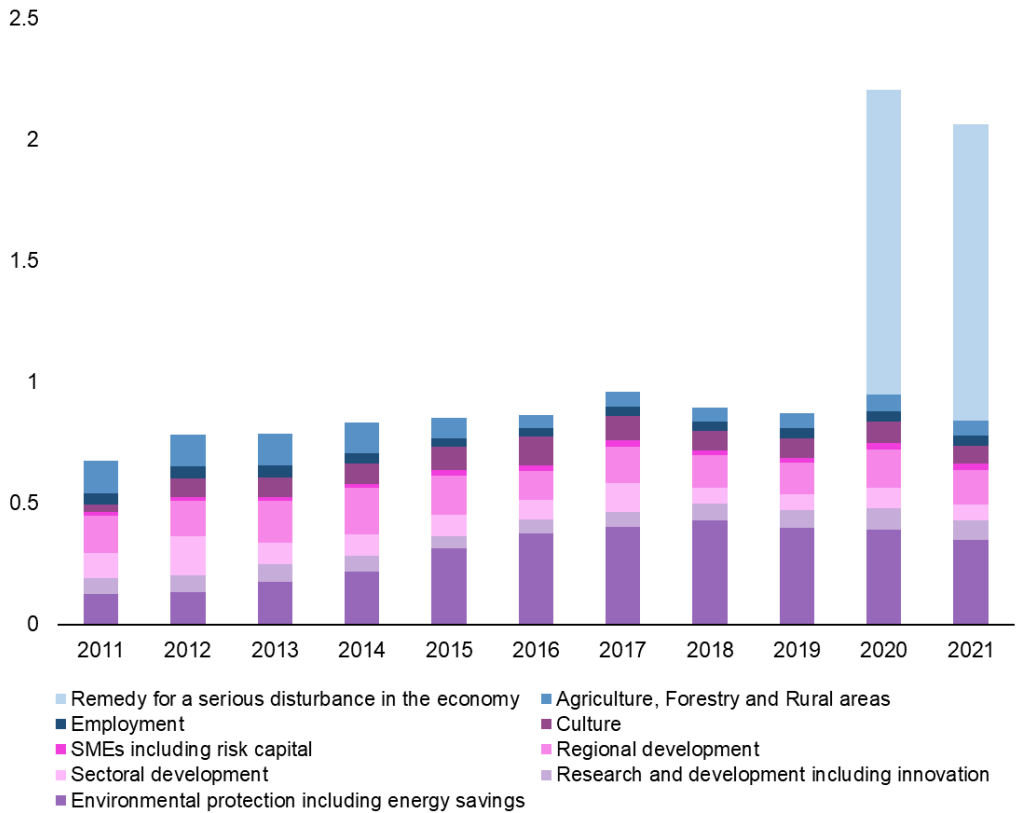


Source: (1) Global Trade Alert. Note: 1/ The number of new policy measures that restrict (harmful) or liberalize trade or FDI introduced in each year. The metric does not account for a measure's intensity. 2/ Cutoff date as of November 22, 2023. (2) Global Trade Alert database, Juhász and others (2022). RHS - Evenett, Jakubik, Martin, and Ruta (2024). (3) GTA NIPO and IMF Estimates

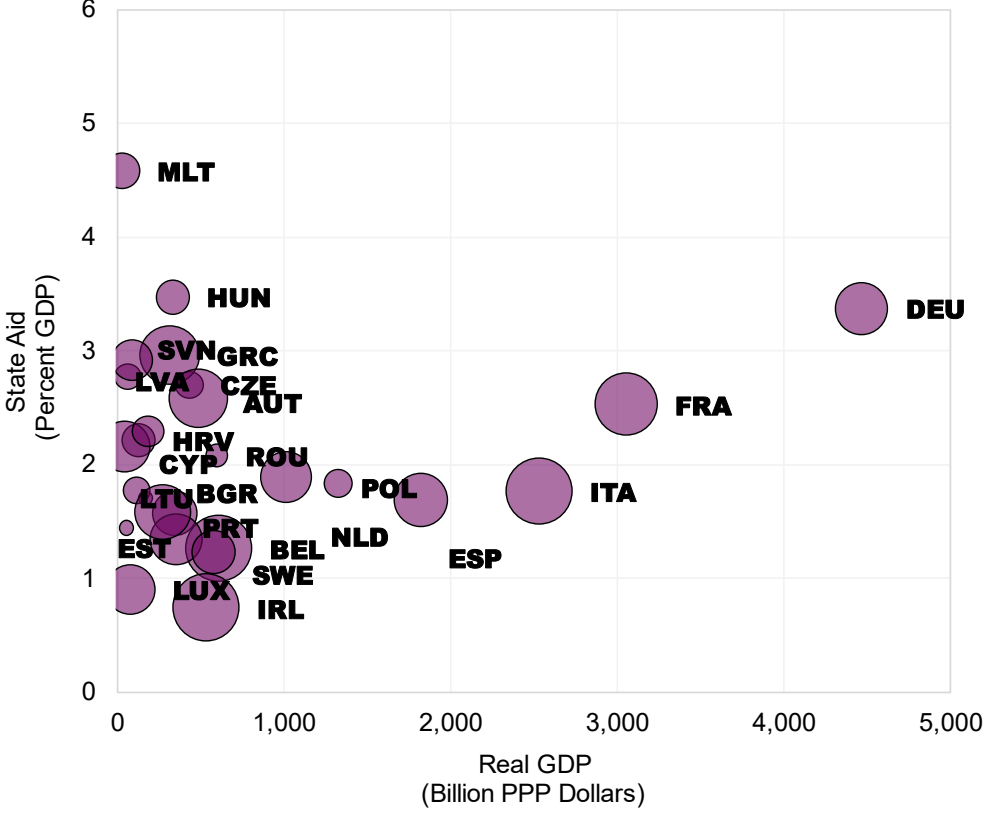


# Relaxation of State Aid

**Average EU State Aid by Select Objectives**  
(Percent of GDP)



**Real GDP and State Aid in 2021**  
(Percent of GDP, Billion PPP Dollars)

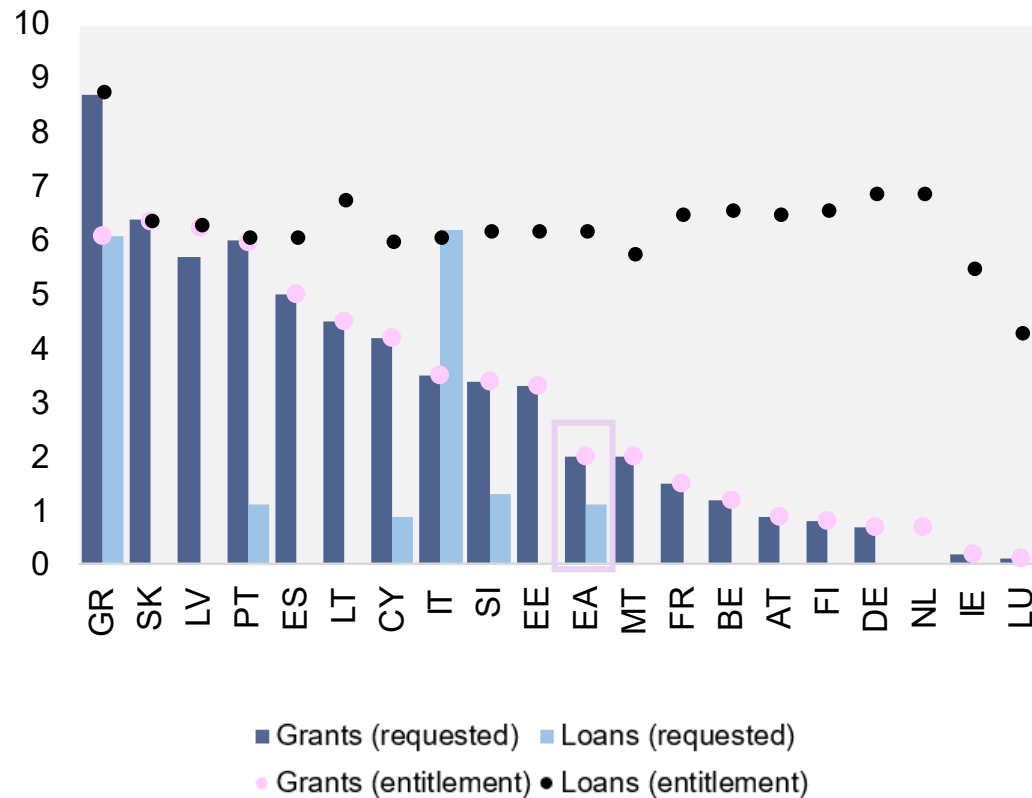


Source: European Commission and IMF staff calculations.

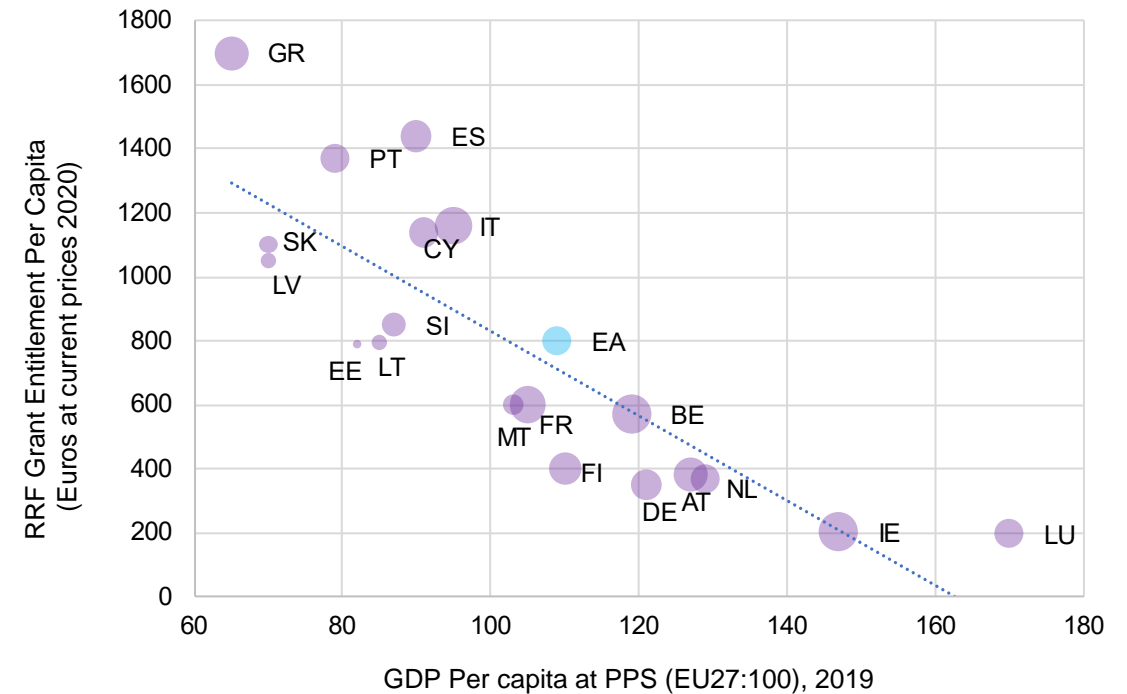
Note: LHS – simple average for the EU. RHS – Bubble size represents general government debt per capita in 2019.

# Next Generation EU

**RRF Entitlements & Funding Requests (2021-26, percentage of 2019 GDP)**



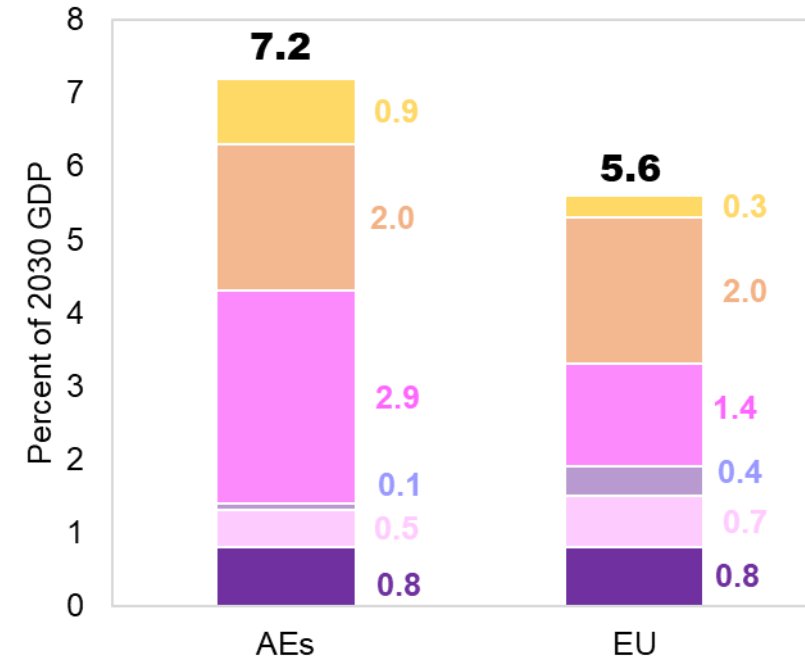
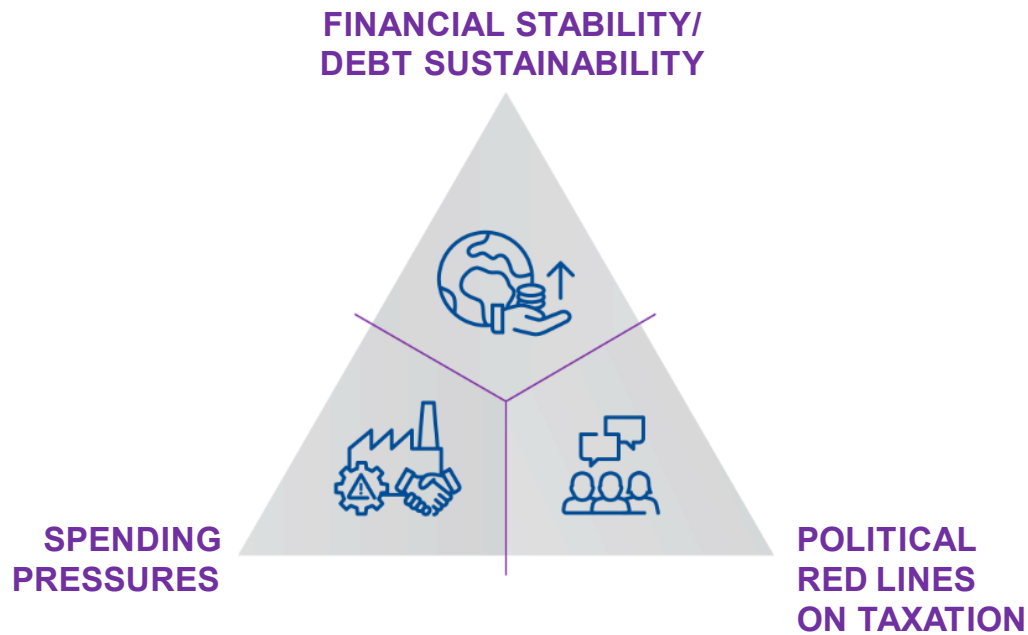
**RRF Grant Entitlement Per Capita (2021-26) & GDP per capita (2019)**



Source: (LHS) ECB Economic Bulletin, Issue 1/2022. (RHS) ECB Economic Bulletin, Issue 1/2022 Notes, IMF World Economic Outlook and IMF Staff Estimates.  
 Note: Bubble size represents general government debt per capita in 2019

# Policy Trilemma – Europe under Rising Geopolitical Tensions

**Pressures to Public Spending**  
(Potential increases by 2030 relative 2023 spending levels)



- Interest payments
- Climate
- Pension and health care
- SDGs
- Defense
- Industrial policy

# Conclusions

- 1 Geopolitics ≠ Globalization**
- 2 The Single Market is a precious asset for competitiveness and growth.**
- 3 Increased salience of geopolitics calls for a European response**
- 4 NGEU has expanded the scope of feasible coordination.**